**Meeting: Council** **Date: 5th February 2015**

**Wards Affected: All Wards in Torbay**

**Report Title: Treasury Management Strategy 2015/16 (incorporating the Annual Investment Strategy 2015/16 and the Minimum Revenue Provision Policy 2015/16)**

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## 1. Purpose and Introduction

1.1 The Strategy outlined in this report aims to support the provision of all Council services by the management of the Council's cash flow, debt and investment operations in 2015/16 and effectively control the associated risks and the pursuit of optimum performance consistent with those risks.

1.2 The overall objectives of the Treasury Management Strategy are:

- To ensure sufficient funding is available for day-to-day activities and capital projects through effective cash flow management
- To seek to reduce the impact on the revenue account of net interest costs through optimal levels of borrowing and investment
- To prioritise control of risks in investing cash and to then achieve maximum returns from those investments commensurate with proper levels of security and liquidity.

## 2. Proposed Decisions

**2.1 That the Treasury Management Strategy for 2015/16 (incorporating the Annual Investment Strategy 2015/16) set out at Appendix 1 to the submitted report be approved;**

**2.2 That the Prudential and Treasury Indicators 2015/16 laid out in Annex 1 of the submitted report be approved;**

**2.3 That in line with the Council's Constitution and Financial Regulations:**

**(i) the Chief Finance Officer be authorised to take any decisions on borrowing and investments. (Delegations to the Section 151 Officer, paragraph 3.1(a));**

**(ii) that the Chief Finance Officer be authorised to invest temporarily or utilise surplus monies of the Council; (Financial Regulations, paragraph 14.5); and**

**(iii) That the provisions outlined above exclude decisions to make loans to external organisations and that these require approval by Council. However loans of less than £50,000 to be approved by the Chief Finance Officer.**

**2.4 That the Annual Minimum Revenue Provision Policy Statement for 2015/16 as shown in Annex 2 to the submitted report be approved.**

## 3. Reason for Decisions

3.1 The Treasury Management Strategy is considered under a requirement of the CIPFA Code of Practice on Treasury Management which was adopted by the Council on 25th March 2010.

3.2 The approval of an Annual Investment Strategy by Council is a requirement of the Guidance on Local Government Investments issued by the Secretary of State under section 15(1)(a) of the Local Government Act 2003. This sets out the Council's policies for managing its investments under the priorities of security first, liquidity second and then returns.

3.3 In addition, the Local Government Act 2003 requires the Council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

3.4 Under CLG regulations the Council is required to approve a Minimum Revenue Provision (MRP) Statement in advance of each year.

3.5 The strategy was considered by 21st January 2015 and in the light of comments made by Members the strategy has been updated.

## Supporting Information

## 4. Position

4.1 The Council defines its treasury management activities as:

***"The management of the authority's investments and cash flows, it's banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".***

4.2 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's risk appetite, providing adequate liquidity initially before considering investment return.

4.3 In particular, Section 32 of the Act requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This report, together with the rolling Capital Investment Plan, forms an integrated strategy to ensure the affordability of capital projects.

4.4 The provisional 2015/16 budget for interest payments has therefore been set at a level which will cover the Council's borrowing requirements in the Capital Investment Plan together with cash flow costs arising from capital projects.

4.5 The interest receipts budget for 2015/16, which is directly linked to the Council's borrowing position, is based on an average investment balance of £64 million and an average investment rate of 0.94% (the estimate for 2014/15 was 0.84%). This includes monies held by the Council's external Fund Manager and exceeds the market benchmark rate forecast to remain at around 0.50%

4.6 The budget for payment of interest on debt for 2015/16 is based on an overall borrowing rate of 4.39% which is unchanged from the previous year.

4.7 The core balances for which cash backing is required reflects the level of Council reserves, provisions, unapplied grants and contributions and working capital. This links to the Capital Investment Plan and Medium Term Resource Plan which form the basis of the Council's longer term strategic cash flow forecasts.

4.8 The proposed strategy for 2015/16 is set out in full at Appendix A to this report and covers the following:

- Prudential and Treasury Indicators;
- Capital expenditure and the Capital Financing Requirement

- the minimum revenue provision (MRP) policy
- core funds and expected investment balances
- prospects for interest rates;
- economic conditions and scenario planning;
- the borrowing strategy;
- the Annual Investment Strategy;
- policy on use of external service providers;
- reporting arrangements and management evaluation;
- other matters

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, CLG MRP Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.

**4.9 The key points of the proposed strategy are:**

* **A slow increase in interest rates with little impact in 2015/16**
* **A steady but slow increase in the level of the Capital Financing Requirement primarily linked to the South Devon Link Road**
* **MRP generates funds per year for repayment of borrowing**
* **The Council will seek to early repay up to £10million of borrowing over the medium term on sufficiently favourable movement in rates**
* **Opportunity to repay will not be assumed within the budget and investment strategy will be based on current projected cash levels;**
* **The number of suitable investment counterparties remains restrictive**
* **An element of core cash levels will, where possible, be exposed to deposits of around one year or longer subject to interest rates and creditworthiness**
* **A proportion of in-house managed funds to be held in short-term variable rate instruments to enact strategy transactions and to mitigate a rise in investment rates.**
* **Options for in-house use of alternative investment instruments are to be investigated following discussions with Audit Committee members. The CFO has identified an option to diversify into a Property Fund and will present this and any other suitable options such as peer-to-peer lending to Council during 2015/16.**
* **The Council's long term liabilities will increase by £33 million when the Energy from Waste capital scheme becomes operational**

## 5. Possibilities and Options

5.1 Not applicable.

## 6. Fair Decision Making

6.1 Not applicable

## 7. Public Services (Social Value) Act 2012

7.1 Not applicable

## 8. Consultation

8.1 Not applicable

## 9. Risks

9.1 The main risks to Treasury Management activities will arise from interest rate levels and volatility, liquidity and cash flow requirements and creditworthiness of investment counterparties.

9.2 The management of specific risks is outlined in the Treasury Management Practices as required by the CIPFA Code of Practice approved by Council on 25th March 2010. Detailed controls are set by the Chief Financial Officer within the Schedules to the Treasury Management Practices and these are reviewed annually.

9.3 Other sections of this report below deal further with risk management and mitigation of particular elements of the 2015/16 Strategy.

**Appendices**

| | |
|---|---|
| Appendix A | Treasury Management Strategy 2015/16 |
| Annex 1 | Prudential and Treasury Management Indicators |
| Annex 2 | Policy on Minimum Revenue Provision for 2015/16 |
| Annex 3 | Interest Rate Forecasts 2015 – 2018 |
| Annex 4 | Economic Background |
| Annex 5 | Creditworthiness Policy |
| Annex 6 | Specified and Non-specified Investments |

**Appendix A**

**Treasury Management Strategy 2015/16**

This Appendix sets out full details for all aspects of the Treasury Management Strategy for 2015/16.

## A1 Prudential Indicators and Treasury Indicators

Local Authorities are required to set indicators to demonstrate they have fulfilled the objectives of the Prudential Code and CIPFA Code of Practice on Treasury Management. The indicators for 2015/16 and future years are set out at Annex1

## A2 Capital Expenditure and the Capital Financing Requirement

A2.1 Capital expenditure plans are a key driver of treasury management activity and form the first of the Prudential Indicators at Annex 1. Figures are as per the Capital Investment Plan Quarter 2 2014/15 report and are summarised below.

| Capital expenditure £M | 2013/14 Actual | 2014/15 Estimate | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|---|
| **Total** | **17.3** | **30.3** | **18.1** | **12.4** | **8.8** | **0** |

A2.2 The figures include a borrowing requirement of £27M over the medium term which includes an element of temporary borrowing awaiting confirmation of capital income.

A2.3 These plans feed into the overall Capital Financing Requirement (CFR) which is explained at Annex 1 and summarised below.

| CFR £M | **2013/14 Actual** | **2014/15 Revised Estimate** | **2015/16 Estimate** | **2016/17 Estimate** | **2017/18 Estimate** | **2018/19 Estimate** |
|---|---|---|---|---|---|---|
| **Total** | **135** | **177** | **178** | **175** | **173** | **TBC** |

## A3 Minimum Revenue Provision (MRP) policy statement

A3.1 The Council is required to set aside an amount for the repayment of borrowing used for capital spend each year (the CFR) through a revenue charge (the minimum revenue provision - MRP). It is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP).

A3.2 CLG regulations have been issued which require the full Council to approve an **MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision.

A3.3 The recommended MRP Policy for 2015/16 is set out at Annex 2 to this report.

## A4 Core funds and expected investment balances

A4.1 The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year end balances for each resource and anticipated day to day cash flow balances.

| Year End Resources £M | 2013/14 Actual | 2014/15 Estimate | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|---|
| Reserves | 37 | 27 | 20 | 15 | 14 | TBC |
| Provisions | 2 | 2 | 2 | 2 | 2 | TBC |
| Other Balances | 1 | 10 | 11 | 13 | 16 | TBC |
| **Total core funds** | **40** | **39** | **33** | **30** | **32** | **TBC** |
| Working capital | 12 | 12 | 12 | 12 | 12 | TBC |
| **Total Cash Requirement** | **52** | **51** | **45** | **42** | **44** | **TBC** |
| Excess LTL>CFR | 12 | 3 | 0 | 1 | (3) | TBC |
| **Expected Investments** | **64** | **54** | **45** | **43** | **41** | **TBC** |

## A5 Prospects for Interest Rates

A5.1 The Council has appointed Capita Asset Services as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. Annex 3 draws together a number of current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following table gives the Capita central view.

| Annual Average % | Bank Rate % | 3 Month LIBID % | PWLB Borrowing Rates % (including certainty rate adjustment) | | |
|---|---|---|---|---|---|
| | | | 5 year | 25 year | 50 year |
| March 2015 | 0.50 | 0.60 | 2.20 | 3.40 | 3.40 |
| March 2016 | 0.75 | 0.90 | 2.60 | 4.00 | 4.00 |
| March 2017 | 1.25 | 1.40 | 3.20 | 4.50 | 4.50 |
| March 2018 | 2.00 | 2.10 | 3.60 | 4.80 | 4.80 |

A5.2 These levels remain low in the short term due to Bank of England policies, market conditions and the impact of quantitative easing.

A5.3 **Sensitivity of Forecasts.** The projections within this report are based on officers "central" view of market rates applicable in 2015/16. These are subject to variation from interest rate changes and cash flow changes. An illustration of the potential impact of these changes is shown in the following table:

| Variation | Central Case | Change +/- | £ Variation* |
|---|---|---|---|
| Change in Investment rates (new investments) | 0.94% | 1% | £0.54 million |
| Change in Borrowing Rates (change in penalty cost on early repayment of an indicative £5 million)** | n/a | 1% | -£0.2million/ +£0.2 million |
| Change in Average cash flow (assume increased investments) | £63 million | £10 million | £0.05 million |

** Based on current levels of borrowing and investment*

***The strategy provides for no additional borrowing in 2015/16 for capital funding and all existing borrowing is at fixed rate so any change in Borrowing Rates will have no effect on interest payable*

A5.4 The above forecasts give rise to difficult conditions for implementing the proposed strategy and the need for Treasury Management officers to remain agile and react to any changes in Bank of England policy or market sentiment.

## A6 Economic Conditions and Scenario Planning

A6.1 A commentary on the economic background to this strategy, issued by Capita, is provided at Annex 4. The uncertainty of economic conditions within the UK and USA appear to be easing but, along with the Eurozone, will continue to have a significant impact on the Council's Treasury Management function.

A6.2 The Council is still facing a situation where Bank Rate and therefore investment returns are at record lows, well below the level payable on borrowings and the focus of the strategy is to mitigate the resultant cost of carrying debt.

A6.3 The Council has linked its medium term financial planning to the continuing uncertain conditions and the impact on the Councils investment budget has formed part of the budget planning process for future years.

A6.4 The current economic conditions are still very unpredictable and as a result there are a range and potential speed of market movements that could occur over the next few years which will provide a challenge to officers. The current strategy and budgets reflect that uncertainty and are based on prudent views of market movements and counterparty limits are set to minimise the Council's exposure to risk.

A6.5 The latent crisis in the Eurozone and the potential effect on markets will continue to be monitored by Officers for threats to treasury activities. The Council currently excludes all Eurozone Banks from the approved lending list regardless of individual credit rating.

A6.6 Varying the Council's counterparty limits could increase or decrease investment yield with a corresponding change in the level of security (risk) over the counterparty. In the current market conditions any extension of counterparty limits and maximum length of investments could increase investment yield. However this would need to be considered against the higher risk of impairment.

A6.7 Diversifying the investment portfolio into more complex instruments could also increase yield but has to be measured in terms of both risk and resource capacity. Options for in-house diversification are being investigated and will be presented to Council in 2015/16.

A6.8 The government has reduced its share in Lloyds Banking Group to 24% and could sell-off a further £3billion in shares in the run up to the next general election. The CFO is satisfied that the current risk appetite for the part-nationalised banks remains appropriate but will adjust exposure limits as appropriate should diminished government stake holding and potential “bail-in” measures increase the investment risk.

A6.9 The charge from the Minimum Revenue Provision policy (see section A3 and Annex 2) generates funds for repayment of borrowing or postponement of new borrowing. Current credit and interest risk environments give rise to a preferred repayment strategy to reduce cost and cash levels.

## A7 Borrowing Strategy

A7.1 The following table provides an analysis of current borrowing levels against the Capital Financing Requirement (CFR) derived from the approved Capital Investment Plan. This also forms one of the Prudential Indicators at Annex 1.

| £m | 2013/14 Actual | 2014/15 Estimate | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|---|
| **External Debt at 31 March** | | | | | | |
| External Borrowing | 138 | 138 | 138 | 138 | 134 | 132 |
| Other long-term liabilities (OLTL)* | 9 | 42 | 40 | 38 | 36 | 34 |
| **Total Borrowing and Other Long Term Liabilities** | **147** | **180** | **178** | **176** | **170** | **166** |
| **The Capital Financing Requirement** | **135** | **177** | **178** | **175** | **173** | **TBC** |

* *The PFI Energy from Waste scheme is required to be shown on-balance sheet and has increased the Council's long-term liabilities by £33million from 2014/15*

A7.2 Prior year strategies to repay borrowing have succeeded in re-aligning the level of borrowing with the CFR.

A7.3 Based on borrowing rate forecasts and continuing low investment yields the recommended strategy aims to further repay existing borrowing and utilise internal cash resources to fund capital expenditure in the short term.

A7.4 The repayment policy remains for any repayment to be made on significant rises in PWLB rates providing advantageous rescheduling opportunities.

A7.5 The trigger for any repayment option will be considered when the payback period of the repayment penalty falls to two years in terms of net interest.

A7.6 The Capital Investment Plan remains fluid and the CFR in A7.1 includes an element of temporary borrowing which may be replaced by other funding thereby reducing the CFR further.

A7.7 At some point in the future the Council will have to re-borrow when internal resources fall below operational cash flow requirements or borrowing reaches maturity, with potential exposure to higher rates. The benefits of the strategy will therefore be weighed against this future interest rate risk.

A7.8 The current market conditions make repayment less attractive due to high penalty costs and these conditions are now forecast to continue further into 2015/16 (see section A5). Budget forecasts for 2015/16 have therefore not assumed the strategy aim to repay borrowing. However, the volatile conditions in the economic climate make predicting rate movements extremely difficult and Officers will act on this strategy at any point the rate environment moves to a favourable position.

A7.9 Based on current PWLB repayment terms, gilt yields need to rise by around 1.10% - 1.50% on the levels as at December 2014 for any repayment to be affordable and by 2.25% to reach the level at which the Council would ideally begin to make repayments.

A7.10 Any repayment of borrowing will only be applied following a thorough assessment of:

- any change to the level of the borrowing requirement
- additional capital projects funded from borrowing
- assessment of working capital and other Council cash backed resources such as Reserves, Provisions and capital grants
- prevailing market conditions
- anticipated cash flow and any temporary borrowing requirements
- future market expectations
- the need to re-borrow in the medium to longer term as loans reach maturity

A7.11 Rescheduling of existing debt will also be considered if opportunities arise, to supplement the primary aim of repaying loans.

A7.12 No new borrowing is envisaged for 2015/16. However, if in future years capital plans significantly change and there is a borrowing need based on internal cash levels, the Council may seek to secure new funding prior to the anticipated rise in borrowing rates in future years.

A7.13 The majority of the Council's cost of interest and associated Revenue Provision relate to historic borrowing "supported" by central government and other debt transferred from Devon County Council on Local Government Reorganisation in 1998. (Borrowing is no longer fully supported due to reductions in Council grant).

A7.14 Borrowing from PWLB or other sources is only one option the Council has to finance its expenditure on capital projects e.g. the Council could use finance leases or provide financing via PFI agreements such as the Energy from Waste Plant.

A7.15 As a matter of policy approved borrowing sources are from the Public Works Loan Board and market instruments from counterparties listed by the Financial Services Authority. The Municipal Bonds Agency, currently in the process of being set up, will also be considered.

## A8 ANNUAL INVESTMENT STRATEGY

### Investment Policy

A8.1 The Council's investment policy has regard to the CLG's Guidance on Local Government Investments and the CIPFA Treasury Management in Public Services Code of Practice.

A8.2 The Council's investment priorities, in line with CLG Guidance, are: -

the security of capital
the liquidity of its investments.

A8.3 The Council will also aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity.

A8.4 The borrowing of monies purely to invest or on-lend and make a return is unlawful and the Council will not engage in such activity.

A8.5 Annex 5 to this report details the policy for selection of counterparties and management of investments to achieve the objectives of the Investment Policy.

A8.6 Investment instruments identified for use in the financial year are listed at Annex 6 under the 'Specified' and 'Non-Specified' Investments categories. Counterparty limits will be set within the schedules accompanying the Council's Treasury Management Practices.

A8.7 In view of the difficult market conditions officers will continue to review alternative investment opportunities for core cash including loans to external organisations. Any loans made under this policy will be classified as policy loans and not a treasury management investment. As such it is recommended that loans of £50,000 and over fall outside of the powers delegated to the CFO and that approval is required by Council.

A8.8 Officers have discussed with members of the Audit Committee, the potential to move into higher risk investments. From initial examination of alternative instruments the CFO has identified an option to diversify part of the investment funds into the CCLA Property Fund. This will be reported to Council in 2015/16 along with other options, such as peer-to-peer lending, to assess any desired shift in risk appetite.

A8.9 The Investment Strategy is based on current projected cash levels. If any significant changes occur to cash levels, e.g. strategy implementation of early repayment of PWLB borrowing, then the Investment Strategy will need to be reviewed.

A8.10 The Council does not adopt a specific Ethical Investments policy but officers will have regard to any questionable activity on the part of a counterparty or sovereign government before depositing funds.

### Investment Strategy

A8.11 The investment strategy for 2015/16 is strongly influenced by the market and credit risks outlined above but needs to be balanced with the need to maximise revenue within these risks.

A8.12 Expected investment levels at A4.1 are subject to increasing risk. Suitable counterparties complying with the Council's selection policy have decreased slightly but remain a limiting factor. Investment rates available to the Council continue to be influenced to the downside due to the effects of Quantitative Easing and Funding for Lending providing cheaper cash for Banks.

A8.13 The strategy driver of using investment cash to repay borrowing (A7.6) to reduce exposure to the interest rate, market and credit risks will continue for 2015/16.

A8.14 The forecast of a slow rise in investments justifies the use of longer term deposits to lock into higher rates and provide guarantee of return in the short term. A total of £15 million is currently locked out to 2016 and any additions will take into account the Trasury Indicator for prudent amounts to be invested for over 364 days as well as liquidity, creditworthiness and interest rate concerns.

A8.15 Current fixed term deposits are predominently in UK part-nationalised banks where the implicit government guarantee continues to offer the safest haven for Council cash. Duration will focus on one year deposits with these institutions to provide a maturity structure that allows officers to respond to reducing cash levels or significant changes in government stakeholding (see A6.8).

A8.16 A proportion of funds will be held in business reserve and notice accounts to ensure appropriate liquidity is maintained for normal cash flow purposes and strategy transactions (eg repayment of borrowing at short notice if PWLB rates move to a favourable position).

A8.17 The Fund Manager's strategy and performance will be subject to continuous monitoring and the CFO will vary the size of the holding in line with the aims of the overall strategy.

## A9 Policy on the use of external advisors

A9.1 The Council currently appoints Capita Asset Services – Treasury Solutions (brand name changed from Sector Treasury Services in 2013) as its external treasury management advisor. The agreement is currently reviewed on an annual basis.

A9.2 The Council recognises the value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Chief Finance Officer will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

A9.3 The Council acknowledges that the responsibility for treasury management decisions remains with the Council at all times and will ensure that undue reliance is not placed upon the external advisors.

## A10 Reporting Arrangements and Management Evaluation

A10.1 Members will receive the following reports for 2015/16 as standard in line with the requirements of the Code of Practice:

- Annual Treasury Management Strategy report (this report)
- Mid-Year Treasury Review report (distributed to Audit Committee and available to all members on the Finance intranet site)
- Annual Treasury Outturn report

A10.2 The CFO will inform the Mayor/Executive Lead for Finance of any long-term borrowing/repayment undertaken or any significant events that may affect the Council's treasury management activities. The CFO will maintain a list of staff authorised to undertake treasury management transactions on behalf of the Council.

A10.3 The Chief Finance Officer is authorised to approve any movement between borrowing and other long-term liabilities within the Authorised Limit. Any such change will be reported to the next meeting of the Council.

A10.4 The impact of these policies will be reflected as part of the Council's revenue budget and therefore will be reported through the quarterly budget monitoring process.

A10.5 The Council's management and evaluation arrangements for Treasury Management will be as follows:

- Monthly monitoring report to the Chief Finance Officer, Executive Lead for Finance, relevant Director and Group Leaders
- Monthly meeting of the Treasury Manager/Chief Accountant to review previous months performance and plan following months activities
- Regular meetings with the Council's treasury advisors
- Annual meetings with the Council's appointed Fund Managers
- Membership and participation in the Capita Benchmarking Clubs
- The Audit Committee is the body responsible for scrutiny of Treasury Management.

## A11 Other Matters

A11.1 **Loans to organisations**. The Council has provided loans or loan facilities to the following organisations. These are policy decisions and not part of the treasury management strategy except for identifying any impact on cash balances:

| Organisation | Value of loan at 01/04/14 | Full Term of Loan | Rate |
|---|---|---|---|
| PLUSS | £139,000 | 15 years | Linked to PWLB rate |
| Torbay Economic Development Company* | £575,000 | 25 years | Linked to Council borrowing Rate |
| Torbay Economic Development Company* | £1,200,000 | 25 years | Linked to Council borrowing Rate |
| Academy Schools | £318,000 | 3 to 7 years | Linked to Council borrowing Rate |
| Car Loans - staff | £4,000 | Repayment expected within 1 year. No new loans issued | Linked to Bank Base Rate |
| Babbacombe Cliff Railway | £16,000 | 10 years | Linked to Council Borrowing Rate |
| Housing Loans | £5,000 | No new loans issued. Term linked to individual mortgages | Linked to market mortgage rates |
| Sports Clubs | £30,000 | 20 years | Linked to Council Borrowing Rate |
| **New Loans in 2014/15** | **Loan Value** | **Term** | **Rate** |
| Sports Clubs | £8,000 | 10 years | Linked to Council Borrowing Rate |
| Suttons Seeds Ltd ** | £1,500,000** | 3 years | Market rate |

*Not drawn down as at 31st December 2014

**Balance of £800,000 not drawn down as at 31st December 2014

A11.2 **Advancing cash**. If approved the Council will advance cash to Torbay Council schools at a rate equivalent to that of the forecast investment yield (to reflect the lost investment opportunity), with the option of an additional 0.25% risk premium. The service will have to identify the funding for this advance from revenue or reserves in the year of the advance.

A11.3 **Investing cash for Local Payment Scheme (LPS) Schools.** If agreed by the Chief Finance Officer the Council will invest LPS school surplus balances on a temporary basis and endeavour to match Bank Rate on these investments on a variable basis. This will be for cash on a longer-term basis and will not apply to daily cash flow balances.

A11.4 **Soft Loans.** New Financial Instruments require the recognition of soft loans i.e. where a loan is made at a lower than ‘competitive’ rate the cost implicit in achieving the lower rate must be reflected in the Council’s accounts.

A11.5 **Anti-Money Laundering.** The Council will comply with all relevant regulations.

A11.6 **Intranet**. The Council’s treasury management procedures and other relevant documents can be accessed on the Council’s intranet site within the financial services pages.

**Annex 1**

**Prudential & Treasury Management Indicators 2014/15 – 2017/18**

## Capital expenditure

This prudential indicator is a summary of the Council's capital expenditure plans (per the Capital Investment Plan Q2 2014/15 report).

| Capital expenditure £M | *2013/14 Actual* | 2014/15 Estimate | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|---|
| **Total** | ***17.3*** | **30.3** | **18.1** | **12.4** | **8.8** | **0** |

## Capital Financing Requirement (CFR)

The CFR is the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need based on historic expenditure. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

The CFR does not increase indefinitely. The minimum revenue provision (MRP) (see section A3) broadly reduces the borrowing need in line with each asset's life.

The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of scheme include a borrowing facility and so the Council is not required to separately borrow for these schemes. The Council currently has £10M of such schemes within the CFR which could rise in 2014/15 if the Councils 17% share of the Energy from Waste liability is accounted for as an "on balance sheet" PFI scheme.

| £m | 2013/14 Actual | 2014/15 Revised Estimate | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2017/18 Estimate |
|---|---|---|---|---|---|---|
| **Capital Financing Requirement** | | | | | | |
| **Total CFR** | **135** | **177** | **178** | **175** | **173** | **TBC** |
| **Movement in CFR** | **(1)** | **42** | **1** | **(3)** | **(2)** | **TBC** |
| **Movement in CFR represented by** | | | | | | |
| Net financing need for the year - capital | 4 | 47* | 7 | 3 | 1 | TBC |
| Less MRP/VRP and other financing movements | (5) | (5) | (6) | (6) | (6) | TBC |
| **Movement in CFR** | **(1)** | **42** | **1** | **(3)** | **(5)** | **TBC** |

*Includes 17% share of costs relating to the Energy from Waste facility in Plymouth

An element of temporary borrowing is included in the above CFR. Capital resources to this amount are expected and once confirmed will therefore reduce the CFR.

## Gross Borrowing & Long term Liabilities and the Capital Financing Requirement

In order to ensure that borrowing will only be for a capital purpose, the Council should ensure that gross external borrowing does not, except in the short term, exceed the total CFR.

| £m | 2013/14 Actual | 2014/15 Estimate | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|---|
| **External Debt at 31 March** | | | | | | |
| External Borrowing | 138 | 138 | 138 | 138 | 134 | 132 |
| Other long-term liabilities (OLTL) | 9 | 42 | 40 | 38 | 36 | 34 |
| **Total Borrowing and Other Long Term Liabilities** | **147** | **180** | **178** | **176** | **170** | **166** |
| **The Capital Financing Requirement** | **135** | **177** | **178** | **175** | **173** | **TBC** |
| **Excess of LTL>CFR** | **12** | **3** | **0** | **1** | **(3)** | **TBC** |

**Affordability Prudential Indicators**

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

**Ratio of financing costs to net revenue stream.**

This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

The ratio rises from 2014/15 onward are due to expected substantial reductions in the Net Revenue Budget requirement measured against fixed costs of borrowing.

| % | 2013/14 Actual | 2014/15 Estimate | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|---|
| Ratio | 8.03 | 8.65 | 9.11 | 9.83 | 9.91 | 10.55 |

**Incremental impact of capital investment decisions on council tax.**

This indicator identifies the revenue costs associated with capital decisions as part of the next year's budget process. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which are not published over a three year period.

| £ | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|
| **Council tax - band D** | 0.00 | 0.00 | 0.00 | 0.00 |

There are no new schemes being presented for approval for 2015/16 and central government has removed supported borrowing. Therefore, there will be no new incremental increases to Council Tax.

However, if temporary borrowing becomes permanent (expected capital receipts and grants are not confirmed) there will then be an incremental impact on the Torbay element of a Band D Council Tax.

Limits on Borrowing and Long-Term Liabilities

***The Operational Boundary*.** This is the limit beyond which external borrowing and long-term liabilities are not normally expected to exceed. In most cases, this would be linked to the CFR, but may be lower or higher depending on the levels of actual borrowing.

| Operational boundary £m | 2014/15 Current | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|
| Borrowing | 138 | 148 | 149 | 145 | 143 |
| Long term liabilities | 42 | 40 | 38 | 36 | 34 |
| Total | 180 | 188 | 187 | 181 | 177 |

***The Authorised Limit for external borrowing and long-term liabilities*.** A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external borrowing is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

| Authorised limit £m | 2014/15 Current | 2015/16 Estimate | 2016/17 Estimate | 2017/18 Estimate | 2018/19 Estimate |
|---|---|---|---|---|---|
| Borrowing | 172 | 167 | 172 | 177 | 182 |
| Other long term liabilities | 42 | 40 | 38 | 36 | 34 |
| Total | 214 | 207 | 210 | 213 | 216 |

## Limits on Activity

There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs/improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;

- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing and are required for upper and lower limits

| Interest rate Exposures | | | | |
|---|---|---|---|---|
| | **2015/16 Upper %** | **2016/17 Upper %** | **2017/18 Upper %** | **2018/19 Upper %** |
| **Limits on fixed interest rates:** | | | | |
| • Debt | 100 | 100 | 100 | 100 |
| • Investments | 80 | 80 | 80 | 80 |
| Limits on variable interest rates: | | | | |
| • Debt | 30 | 30 | 30 | 30 |
| • Investments | 75 | 75 | 75 | 75 |

| Maturity Structure of fixed interest rate borrowing 2015/16 | | | |
|---|---|---|---|
| | **Lower** | **Upper** | **Expected 31/03/2015** |
| Up to 10 years | 5% | 50% | 14% |
| 10 to 20 years | 5% | 50% | 19% |
| 20 to 30 years | 10% | 60% | 26% |
| 30 to 40 years | 10% | 50% | 25% |
| Over 40 years | 0% | 50% | 17% |

**<u>Investment Treasury Indicator and Limit</u>**

Total principal funds invested for greater than 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end. The limits below allow for the external Fund Manager holding along with 50% of the in-house total to be fixed longer term.

| Maximum principal sums invested for over 364 days | | | | | |
|---|---|---|---|---|---|
| **£m** | **2014/15** | **2015/16** | **2016/17** | **2017/18** | **2018/19** |
| Principal sums invested > 364 days | 45 | 51 | 46 | 37 | 37 |

**Annex 2**

## Policy on Minimum Revenue Provision for 2015/16

1. The Minimum Revenue Provision is a statutory charge that the Council is required to make from its revenue budget. This provision enables the Council to generate cash resources for the repayment of borrowing.

2. The calculation of the provision is prescribed by legislation, which states that Councils are required to "determine for the current financial year an amount of MRP that it considers to be prudent" and prepare an annual statement on their MRP calculation to their full Council.

3. One of the aims of this legislation is to ensure that the repayment of principal owed for capital expenditure funded from unsupported borrowing is charged on a prudent basis which closely links to the asset's life. The provision for all assets, irrespective of asset life, for expenditure funded from supported borrowing and prudential borrowing prior to 2007/08 will continue to be charged at a minimum 4% per annum which is in line with central government's "support" for these costs within the Council's formula grant.

4. Torbay Council's Annual Minimum Revenue Provision Policy Statement states that the calculation of the MRP is as follows which has 2 stages:

    i) The Council will budget as a minimum for a provision of 4% of its capital financing requirement calculated as at 31st March of the preceding financial year. The capital financing requirement (CFR) is a calculation of a Council's "need to borrow" which is, in summary, the total of expenditure funded from borrowing less any repayments or similar previously made.

    To calculate the 4% provision the Council will use the "regulatory method" as identified in the Department of Communities and Local Government's (DCLG) Informal Commentary on the legislation.

    This calculation allows for the adjustments of the following items:

    - Deducting any expenditure and revenue provision made in relation to unsupported borrowing after 2007/08. The charge for unsupported borrowing after 2007/08 is calculated separately as described in paragraph ii below.
    - "Adjustment A" which relates to a previous calculation change in 2004
    - Adjustment of MRP to ensure no disadvantage results to Councils from the regulations compared to previous MRP regulations
    - Adjustment of MRP to ensure no disadvantage results to Councils from the requirements for accounting for Finance Lease and Private Finance Initiative schemes

ii) For capital expenditure funded from unsupported or prudential borrowing less any repayment to date, the Council will make a provision based on the cumulative expenditure incurred on each asset in the previous financial years using a prudent asset life, which reflects the estimated usable life of that asset.

The Council will use the “asset life method” for the calculation, the MRP for each asset will be calculated using an annuity calculation based on the Council’s estimated pooled borrowing interest rate for the relevant year as detailed in the Treasury Management Strategy for that year. This will be adjusted for:-

- An adjustment to the MRP calculation will be made where there is expenditure in the previous financial year, but the asset is not yet operational. MRP will be calculated on the total expenditure on that asset in the year after the asset becomes operational.

5) Where relevant, the suggested asset lives for certain types of capitalised expenditure as detailed in the MRP guidance issued by DCLG will be used.

6) The Council will continue to charge services for their use of unsupported borrowing using a prudent asset life (or a shorter period) and an annuity calculation. Where possible the same asset life and borrowing interest rate will be used for both the charge to services and the calculation of the MRP.

7) In exceptional circumstances a Service may be allowed to extend the repayment period beyond the prudent asset life but this may be limited to the interest element. The increased revenue cost over the longer term will be a Service issue.

8) Where assets prior to 2007/08 have been purchased by unsupported borrowing (before the current legislation applied) and a MRP at 4% is provided for, the Council will aim, over the long term, to balance the annual costs of the MRP on these assets with the repayments made by services. This may result in a Voluntary Revenue Provision (VRP) or reserve transfer being made.

9) The Council will not change its existing “Adjustment A” calculation.

10) To mitigate any negative impact from the changes in accounting for leases and PFI schemes the Council will include in the annual MRP charge an amount equal to the amount that has been taken to the balance sheet to reduce the balance sheet liability for a PFI scheme or a finance lease. The calculation will be based on the annuity method using the Internal Rate of Return (IRR) implicit in the PFI or lease agreement.

11) In relation to borrowing transferred to the Council from Devon County Council for the Council’s share of the Devon County Council debt for local government reorganisation, the Council will budget to make a VRP over 40 years to ensure cash resources for the repayment of the debt is available on maturity.

12) <u>Loans</u>

Where loans are given for capital purposes they come within the scope of the prudential controls established by the Local Government Act 2003. Regulation 25(1)(b) of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (SI 2003 No 3146).

If a loan agreement does not include contractual commitments that the funds be put towards capital expenditure no MRP will be made, if however capital contract commitments are included then an MRP will be made on a prudent basis using Option 3 (annuity Basis) linked to the life of the asset being funded.

The Capital Financing Requirement (CFR) will increase by the amount of the loan. Once the funds are returned to the local authority, the returned funds are classed as a capital receipt with those receipts being earmarked specifically to that loan, and the CFR and loan will reduce accordingly. As this is a temporary arrangement and the expectation is that funds will be returned in full, there is no need to set aside prudent provision to repay the debt liability in the interim period, so there is no MRP application. The position will be reviewed on an annual basis.

Annex 3

# Interest Rate Forecasts 2014 – 2018 (as at December 2014)

| Capita Asset Services Interest Rate View | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Mar-15 | Jun-15 | Sep-15 | Dec-15 | Mar-16 | Jun-16 | Sep-16 | Dec-16 | Mar-17 | Jun-17 | Sep-17 | Dec-17 | Mar-18 |
| Bank Rate View | 0.50% | 0.50% | 0.50% | 0.75% | 0.75% | 1.00% | 1.00% | 1.25% | 1.25% | 1.50% | 1.75% | 1.75% | 2.00% |
| 3 Month LIBID | 0.50% | 0.50% | 0.60% | 0.80% | 0.90% | 1.10% | 1.10% | 1.30% | 1.40% | 1.50% | 1.80% | 1.90% | 2.10% |
| 6 Month LIBID | 0.70% | 0.70% | 0.80% | 1.00% | 1.10% | 1.20% | 1.30% | 1.50% | 1.60% | 1.70% | 2.00% | 2.10% | 2.30% |
| 12 Month LIBID | 0.90% | 1.00% | 1.10% | 1.30% | 1.40% | 1.50% | 1.60% | 1.80% | 1.90% | 2.00% | 2.30% | 2.40% | 2.60% |
| 5yr PWLB Rate | 2.20% | 2.20% | 2.30% | 2.50% | 2.60% | 2.80% | 2.90% | 3.00% | 3.20% | 3.30% | 3.40% | 3.50% | 3.60% |
| 10yr PWLB Rate | 2.80% | 2.80% | 3.00% | 3.20% | 3.30% | 3.50% | 3.60% | 3.70% | 3.80% | 3.90% | 4.00% | 4.10% | 4.20% |
| 25yr PWLB Rate | 3.40% | 3.50% | 3.70% | 3.80% | 4.00% | 4.20% | 4.30% | 4.40% | 4.50% | 4.60% | 4.70% | 4.70% | 4.80% |
| 50yr PWLB Rate | 3.40% | 3.50% | 3.70% | 3.80% | 4.00% | 4.20% | 4.30% | 4.40% | 4.50% | 4.60% | 4.70% | 4.70% | 4.80% |
| **Bank Rate** | | | | | | | | | | | | | |
| Capita Asset Services | 0.50% | 0.50% | 0.50% | 0.75% | 0.75% | 1.00% | 1.00% | 1.25% | 1.25% | 1.50% | 1.75% | 1.75% | 2.00% |
| Capital Economics | 0.50% | 0.50% | 0.75% | 0.75% | 1.00% | 1.00% | 1.25% | 1.25% | - | - | - | - | - |
| **5yr PWLB Rate** | | | | | | | | | | | | | |
| Capita Asset Services | 2.20% | 2.20% | 2.30% | 2.50% | 2.60% | 2.80% | 2.90% | 3.00% | 3.20% | 3.30% | 3.40% | 3.50% | 3.60% |
| Capital Economics | 2.20% | 2.50% | 2.70% | 3.00% | 3.10% | 3.20% | 3.30% | 3.40% | - | - | - | - | - |
| **10yr PWLB Rate** | | | | | | | | | | | | | |
| Capita Asset Services | 2.80% | 2.80% | 3.00% | 3.20% | 3.30% | 3.50% | 3.60% | 3.70% | 3.80% | 3.90% | 4.00% | 4.10% | 4.20% |
| Capital Economics | 2.80% | 3.05% | 3.30% | 3.55% | 3.60% | 3.65% | 3.70% | 3.80% | - | - | - | - | - |
| **25yr PWLB Rate** | | | | | | | | | | | | | |
| Capita Asset Services | 3.40% | 3.50% | 3.70% | 3.80% | 4.00% | 4.20% | 4.30% | 4.40% | 4.50% | 4.60% | 4.70% | 4.70% | 4.80% |
| Capital Economics | 3.25% | 3.45% | 3.65% | 3.85% | 3.95% | 4.05% | 4.15% | 4.25% | - | - | - | - | - |
| **50yr PWLB Rate** | | | | | | | | | | | | | |
| Capita Asset Services | 3.40% | 3.50% | 3.70% | 3.80% | 4.00% | 4.20% | 4.30% | 4.40% | 4.50% | 4.60% | 4.70% | 4.70% | 4.80% |
| Capital Economics | 3.30% | 3.50% | 3.70% | 3.90% | 4.00% | 4.10% | 4.20% | 4.30% | - | - | - | - | - |

Please note – The current PWLB rates and forecast shown above have taken into account the 20 basis point certainty rate reduction effective as of the 1st November 2012

**Annex 4**

**Economic Background (provided by Capita Asset Services on 7th January 2015)**

**UK** GDP growth surged during 2013 and the first half of 2014. Since then it appears to have subsided somewhat but still remains strong by UK standards and is expected to continue likewise into 2015 and 2016. There needs to be a significant rebalancing of the economy away from consumer spending to manufacturing, business investment and exporting in order for this recovery to become more firmly established.

One drag on the economy has been that wage inflation has only recently started to exceed CPI inflation, so enabling disposable income and living standards to start improving. The plunge in the price of oil brought CPI inflation down to a low of 1.0% in November, the lowest rate since September 2002. Inflation is expected to stay around or below 1.0% for the best part of a year; this will help improve consumer disposable income and so underpin economic growth during 2015.

However, labour productivity needs to improve substantially to enable wage rates to increase and further support consumer disposable income and economic growth. In addition, the encouraging rate at which unemployment has been falling must eventually feed through into pressure for wage increases, though current views on the amount of hidden slack in the labour market probably means that this is unlikely to happen early in 2015.

The **US**, the biggest world economy, has generated stunning growth rates of 4.6% (annualised) in Q2 2014 and 5.0% in Q3. This is hugely promising for the outlook for strong growth going forwards and it very much looks as if the US is now firmly on the path of full recovery from the financial crisis of 2008. Consequently, it is now confidently expected that the US will be the first major western economy to start on central rate increases by mid 2015.

The current economic outlook and structure of market interest rates and government debt yields have several key treasury management implications:

- **Greece:** the general election on 25 January 2015 is likely to bring a political party to power which is anti EU and anti austerity. However, if this eventually results in Greece leaving the Euro, it is unlikely that this will directly destabilise the Eurozone as the EU has put in place adequate firewalls to contain the immediate fallout to just Greece. However, the indirect effects of the likely strengthening of anti EU and anti austerity political parties throughout the EU is much more difficult to quantify;

- As for the **Eurozone** in general, concerns in respect of a major crisis subsided considerably in 2013. However, the downturn in growth and inflation during the second half of 2014, and worries over the Ukraine situation, Middle East and Ebola, have led to a resurgence of those concerns as risks increase that it could be heading into deflation and prolonged very weak growth. Sovereign debt difficulties have not gone away and major concerns could return in respect of individual countries that do not dynamically address fundamental issues of low growth, international uncompetitiveness and the need for overdue reforms of the economy (as Ireland has done). It is, therefore, possible over the next few years that levels of government debt to GDP ratios could continue to rise to levels that could result in a loss of investor confidence in the financial viability of such countries. Counterparty risks therefore remain elevated. This continues to suggest the use of higher quality counterparties for shorter time periods;

- Investment returns are likely to remain relatively low during 2015/16 and beyond;

- Borrowing interest rates have been volatile during 2014 as alternating bouts of good and bad news have promoted optimism, and then pessimism, in financial markets. The closing weeks of 2014 saw gilt yields dip to historically remarkably low levels after inflation plunged, a flight to quality from equities (especially in the oil sector), and from the debt and equities of oil producing emerging market countries, and an increase in the likelihood that the ECB will commence quantitative easing (purchase of EZ government debt) in early 2015. The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in later times, when authorities will not be able to avoid new borrowing to finance new capital expenditure and/or to refinance maturing debt;

- There will remain a cost of carry to any new borrowing which causes an increase in investments as this will incur a revenue loss between borrowing costs and investment returns.

**Annex 5**

**Creditworthiness Policy**

1. This Council applies the creditworthiness service provided by Capita Asset Services. This service employs a sophisticated modelling approach utlilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings are supplemented by with the following overlays:

    - Credit watches and credit outlooks from the credit rating agencies
    - Credit Default Swap (CDS) spreads to give early warning of likely changes in credit ratings
    - Sovereign ratings to select counterparties from only the most creditworthy countries

2. This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of Credit Default Swap (CDS) spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. The Chief Finance Officer applies and reviews suitable financial and durational limits to each of these bands.

3. A specific creditworthiness colour band has been created for UK part-nationalised Banks which is based upon the implicit sovereign government guarantee in these institutions in place of their individual credit ratings.

4. Continuing regulatory changes in the banking sector are designed to see greater stability, lower risk and the removal of expectations of Government financial support should an institution fail. This withdrawal of implied sovereign support is anticipated to have an effect on ratings applied to institutions. This will result in the key ratings used to monitor counterparties being the Short Term and Long Term ratings only. Viability, Financial Strength and Support Ratings previously applied will effectively become redundant. This change does not reflect deterioration in the credit environment but rather a change of method in response to regulatory changes.

5. The Capita creditworthiness service uses a wider array of information than just primary ratings and by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.

6. Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

7. All credit ratings will be monitored on a weekly basis. The Council is alerted to changes to ratings of all three agencies through its use of the Capita creditworthiness service and the CFO will vary the approved lending list as appropriate to these changes.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

8. The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA+.The list of countries that qualify using this credit criteria as at the date of this report (based on the lowest available rating) are shown below and this list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

| **AAA** | | **AA+** |
|---|---|---|
| Australia | Norway | Finland |
| Canada | Singapore | Hong Kong |
| Denmark | Sweden | Netherlands |
| Germany | Switzerland | United Kingdom |
| Luxembourg | | USA |

9. Sole reliance will not be placed on the use of this external service. In addition the CFO will also use market data and market information, information on government support for banks and the credit ratings of that government support.

10. The Council uses an external fund manager to manage a proportion of the investment portfolio available to offset the borrowing requirement. The use of an external fund manager allows the Council to spread its treasury risk in relation to type of investment, investment counterparties and manager opinion.

11. The external fund manager will comply with the Annual Investment Strategy. The agreement between the Council and the fund manager additionally stipulates guidelines and duration and other limits in order to contain and control risk.

12. The fund manager mandate allows for additional amounts to be placed and the CFO will exercise this option if this is deemed to be in the best interests of the Council up to a limit of 50% of the total portfolio. As Council's cash investment reduce it is likely the Fund Manager holding will be correspondingly decreased. The Council retains the right to withdraw all or part of the fund at seven days notice.

**Annex 6**

**Specified and Non-Specified Investments**

Investments types recorded in bold type are the instruments most commonly used by the in-house team.

**SPECIFIED INVESTMENTS:** All such investments will be sterling denominated, with **maturities up to maximum of 1 year**, meeting the minimum 'high' quality criteria where applicable.

| | **Minimum 'High' Credit Criteria** | **Use** |
|---|---|---|
| **Debt Management Agency Deposit Facility** | **--** | **In-house** |
| **Term deposits – local authorities and other public sector bodies** | **--** | **In-house** |
| **Term deposits – banks and building societies** | **Creditworthiness system colour band "Green"** | **In-house and Fund Manager** |
| **UK nationalised/part-nationalised banks** | **--** | **In-house and Fund Manager** |
| **Banks part-nationalised by high credit rated (sovereign rating) countries – non UK** | **Sovereign rating AA+** | **In-house and Fund Manager** |
| **Collective Investment Schemes structured as Open Ended Investment Companies (OEICs): -**<br>**1. Government Liquidity Funds**<br>**2. Money Market Funds** | **AAA** | **In-house and Fund Manager** |

**NON-SPECIFIED INVESTMENTS**: These are any investments which do not meet the Specified Investment criteria.

A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the above categories.

The maturity limits recomended will not be exceeded. Under the delegated powers the Chief Finance Officer can set limits that are lower based on the latest economic conditions and credit ratings.

| **Investment Type** | **Minimum Credit Criteria** | **Use** | **Max % of total investments** | **Max. maturity period *** |
|---|---|---|---|---|
| UK nationalised/part-nationalised banks (maturities over one year) | Sovereign rating AA+ | In-house and Fund Manager | 50% | 3 years |
| Term deposits (over one year) – local authorities and other public sector bodies | -- | In-house | 50% | 5 years |
| Term deposits (over one year) – banks and building societies | Creditworthiness system colour band “Purple” | In-house and Fund Manager | 75% | 2 years |
| Collateralised deposit | See note 1 | In-house | 20% | 5 years |
| Certificates of deposits issued by banks and building societies (maturities under one year) | Creditworthiness system colour band “Green” | In-house and Fund Manager | 50% | 1 year |
| Certificates of deposits issued by banks and building societies (maturities over one year) | Creditworthiness system colour band “Purple” | In-house and Fund Manager | 50% | 1 year |
| UK Government Gilts/Treasury Bills | Sovereign rating AA+ | In-house and Fund | 100% | 5 years |

| Investment Type | Minimum Credit Criteria | Use | Max % of total investments | Max. maturity period * |
|---|---|---|---|---|
| | | Manager | | |
| Bonds issued by multilateral development banks | AA+ | In-house and Fund Manager | 50% | 5 years |
| Sovereign bond issues (other than the UK govt) | Sovereign rating AA+ | In-house and Fund Manager | 50% | 5 years |
| **Structured Deposits** | **Creditworthiness system colour band "Orange" <1 year "Purple" >1 year** | **In-House** | **25%** | **2 years** |
| Commercial paper issuance by UK banks covered by UK Government guarantee | Sovereign rating AA+ | Fund Manager | 35% | 5 years |
| Commercial paper other | Creditworthiness system colour band "Red" | Fund Manager | 35% | 5 years |
| Floating Rate Notes | Long-term AA | In-house and Fund Manager | 35% | 5 years |
| Property Fund: *the use of these investments would normally constitute capital expenditure* | -- | In-house and Fund Manager | 35% | 5 years |
| Property Fund: *not classified as capital expenditure* | | In-house | 20% to a maximum of £10million | 5 years |
| Collective Investment Schemes structured as Open Ended Investment Companies (OEICs):**-**<br>1.Bond Funds<br>2.Gilt Funds | AAA | Fund Manager | 35% | 5 years |

| Investment Type | Minimum Credit Criteria | Use | Max % of total investments | Max. maturity period * |
|---|---|---|---|---|
| Corporate Bonds | AA | In-house and Fund Manager | 35% | 5 years |
| Other debt issuance by UK Banks covered by UK Government guarantee | Sovereign rating AA+ | In-house and Fund Manager | 35% | 5 years |

*Of which in any class of investment:

- 10% maximum 3 years (or over)
- 25% maximum 2 to 3 years

Notes

1. As collateralised deposits are backed by collateral of AAA rated local authority LOBOs, this investment instrument is regarded as being a AAA rated investment as it is equivalent to lending to a local authority.